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ANALYSIS OF THE SCOTTISH DRAFT BUDGET 2015-16

Big picture

The overall profile of austerity that the UK government is embarked on, and which impinges heavily on the profile of the Scottish Budget via the Barnett formula, suggests that 2015-16 is likely to prove to be one of the milder years in terms of cuts.

For financial year 2015-16, the real terms (i.e., inflated adjusted) cut is given in the new Scottish Budget as -1.7%. This is considerably lower than the -3% to -5% real terms cuts seen in both 2010-11 and 2011-12 and than the cuts of over -3% that are likely to re-emerge in both 2016-17 and 2017-18.

Portfolio Settlements

Our analysis concentrates on the largest Portfolios and the biggest changes to Portfolio budgets.

<u>Health and the NHS</u>

The Health budget, via the protected NHS budget, receives one of the largest Portfolio increases, rising by over £200 million (1.7%), 2015-16 on 2014-15. This is also shown in the draft Budget as an increase in <u>real</u> terms of £17 million (equivalent to 0.1 of a percentage point).

Within Health, the NHS budget in 2015-16 is planned to rise by £233 million (2.5%) in cash terms, a real terms increase of £82 million (0.9%). This is largely unchanged from last years Budget plans. The increase incorporates the Barnett related additional funding resulting from the increase seen in the English NHS spending, as well as previously planned additional funding of £86 million.

Outside of the NHS, an extra £54 million, on top of what was previously proposed for 2015-16, will go to further promoting the integration of health and social care. However, the 'Other' health budget (i.e., excluding the NHS), as a whole, still falls in cash terms.

There are a number of important caveats around the degree of 'protection' against inflation implied by these figures.

The inflation measure used by the Scottish government relates to the GDP deflator, which is estimated to be 1.6% by HM Treasury for 2015-16. However, possible alternative measures of inflation would have been higher. For example, for the same year, HM Treasury estimate the Consumer Price Index (CPI) to be 2.0%, the Retail Price Index (RPI) to be 3.3% and the 'triple lock' guarantee (that applies to the uprating of pensions) also to be 3.3%.

Furthermore, the Scottish government guarantee only applies to day-to-day (i.e., resource) spending on the NHS and Special Boards budget. It does not extend to capital spending. Neither does it cover day-to-day spending on Primary and Community Care Services (which includes General Medical Services, Dental Services and Opthalmic Services), whose budgets remains flat in cash terms and so falling in real terms.

The UK government's NHS 'protection' promise extends to a wider definition of English health spending, which is why the Institute of Fiscal Studies recently found the Scottish NHS budget to be growing more slowly, in % terms though not necessarily in cash terms, than the English NHS budget.

Even if the same definitions of NHS spend were being used by the Scottish and UK governments it should not be surprising that the degree of 'protection' for the NHS in Scotland differs from that seen for the NHS in England. As Scotland starts off with a higher spend per person than England (by about 10%), if the same cash terms increase, per person, is applied to both (as delivered via the Barnett formula) then this will equate to a lower % terms increase in Scotland.

Local Government (LG)

In comparison to 2014-15, the General Resource Grant received by LG from the Scottish government for 2015-16 is close to flat in cash terms (-£40 million) and down by £156 million (-2.2%) in real, inflation-adjusted, terms.

However, this figure is around £200 million higher than what was proposed in last year's draft Budget for 2015-16. The increase principally involves extra funding for free primary school meals (£54 million) and pre school entitlement (£44 million). This increase was also affected by an £85 million increase in the Grant which is intended to offset a decline in NDRI of the same amount.

The total amount available for LG to spend includes non domestic rates income (NDRI). When this sum is added, along with capital spend, then overall LG funding for 2015-16 rises by about £170 million (1.6%) over 2014-15. In real, inflation adjusted, terms this measure remains flat.

Infrastructure, Investment and Cities

There is a £300 million increase on the Budget for 2015-16 and a £180 million increase on what had previously been budgeted for that year. This was mainly due to a £200 million increase in the Housing and Regeneration budget.

New Powers

The Scotland Act taxes (Land and Buildings Transactions Tax (LBTT) and Scottish Landfill Tax (SLT)) are projected to raise £558 million in 2015-16, roughly 2% of the total Scottish Budget. This is a similar sum of money as the existing taxes currently raise, although the distribution of who pays will change.

There will be a cut in the Scottish government's Block grant from Westminster to adjust for these new powers, although the exact mechanism by which this adjustment will be made is still to be finalised.

One interesting aspect of the implementation of the LBTT is that it highlights the narrowness of differentials in Council Tax (CT) charges across houses of different value. For example, while CT only doubles when moving from Band D to the top Band H, the shift in LBTT rates increases payments 38-fold between a house worth £250,000 and one worth £1 million. If the LBTT charging system is in line with ‘fairness, equity and the ability to pay’, then it brings into question how well that description applies to the CT system. Of course such a discrepancy existed before, using the old Stamp Duty system, but not to the same degree and not imposed by a Scottish government.

The new borrowing powers for 2015-16 are limited to £304 million and these are to be used in full. The Scottish government can borrow from the National Loans Fund, from banks on commercial terms, or through issuing bonds. No decision has yet been made on which method(s) to use.

It is assumed that the new borrowing will be long term in nature (i.e., with repayment over 25-years) and that an interest rate of 5 per cent is charged, which covers repayment of both interest charges and principal. However, actual costs are yet to be negotiated with HMT (or any other proposed funder).

Public Sector Pay

The Scottish government will continue to implement the two year pay policy introduced for 2014-15. The key features of this were a 1 per cent cap on the increase in basic pay (except for those earning under £21,000) and a policy of no compulsory redundancies.

Further analysis

Fiscal Affairs Scotland will be undertaking further analysis in the near future which will look in more detail at some of the issues discussed above as well as at the bigger picture of what cuts are still to come.

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